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THE INTERSECTION OF OPPRESSION, MISMANAGEMENT, AND CORPORATE RESTRUCTURING: LEGAL IMPLICATIONS FOR MINORITY SHAREHOLDER

AUTHORED BY - RISHIT

Abstract

Corporate restructuring plays a pivotal role in enabling companies to align their operations with prevailing economic trends and meet internal strategic objectives. By reconfiguring their structure, organizations can optimize efficiency, reduce operational redundancies, and benefit from economies of scale, thereby enhancing overall competitiveness. However, while corporate restructuring can unlock significant growth opportunities, it may also pose substantial risks, particularly for minority shareholders.

The terms and conditions governing restructuring processes are critical in determining their outcomes. A well-executed restructuring plan can lead to improved governance and long-term financial sustainability. However, poorly drafted or inequitable restructuring agreements may result in the erosion of minority shareholders' rights, leaving them vulnerable to unfair treatment. This is especially pertinent in cases where decision-making power is concentrated in the hands of majority stakeholders, potentially leading to decisions that prioritize their interests over those of minority shareholders.

This research paper examines the dual-edged nature of corporate restructuring, highlighting its potential to both foster growth and create adverse consequences for minority shareholders. It explores the legal and regulatory frameworks that aim to safeguard shareholder rights and prevent abuse during restructuring processes. Furthermore, the study delves into case studies to illustrate the real-world impacts of restructuring decisions on minority stakeholders, drawing attention to the need for transparency, fairness, and accountability.

By focusing on the intricate balance between the benefits of restructuring and the protection of minority interests, this paper underscores the importance of robust governance mechanisms. It advocates for legal safeguards that ensure equitable treatment of all shareholders, regardless of their stake size, thereby fostering a fair and inclusive corporate environment.

The research paper seeks to answer the following questions:

- i. What is the scope of ‘oppression’ and ‘mismanagement’ under the Companies Act, 2013?
- ii. How can Corporate Restructuring lead to the oppression of minority shareholders’ rights?
- iii. What legal recourses do minority shareholders have, and what reforms are required to protect their rights?

Introduction

A company’s internal governance system reflects that of a democracy in the fact that decisions are taken via votes cast by all members, and the direction opted is the one towards which the majority votes. Decisions will be taken by either a simple majority or a special majority, depending on the nature of the decision, binding all the members and shareholders. The differing interests, if any, of the minority shareholders, will be safeguarded as far as possible. Such decision-making is meant to put collective interests over individual ones. The ideal set-up comes crashing down when the majority of stakeholders start acting undemocratically by favouring their own interests over the larger interests.

Bringing about appropriate provisions for safeguarding the interests of the minority shareholders was a key driving force behind the Companies Act, 2013 (“CA, 2013”).¹ Section 241-246 under Chapter XVI of the CA, 2013 deals with oppression and mismanagement in a company setting. It aims to protect and offer redressal to minority shareholders against oppression and mismanagement by the majority. The remedies for the protection of minority shareholders were first introduced in India by the Indian Companies (Amendment) Act, 1951², followed by the Companies Act, 1956 (“CA, 1956”)³, and culminated in the CA, 2013, as we have it now. It brought about an overhaul within the Indian corporate law regime.

The CA, 2013 dissolved the erstwhile Company Law Board (“CLB”), established under CA, 1956, and constituted the National Company Law Tribunal (“NCLT”) and National Company Law Appellate Tribunal (“NCLAT”) under Sections 408⁴ and 410⁵ respectively. They have

¹ The Companies Act 2013.

² The Companies (Amendment) Act 1951.

³ The Companies Act 1956.

⁴ The Companies Act 2013.

⁵ Ibid, s 410.

been vested with exclusive jurisdiction to deal with cases arising out of the CA, 2013 to ensure streamlined and speedy disposal of cases. Under Section 430, jurisdiction of civil courts has been excluded.⁶ With the CA, 2013 coming into effect, all proceedings pending under the CA, 1956, stood transferred to the NCLT. This includes all proceedings pending before any Court below the Supreme Court.⁷ These matters remain arbitrable in many major jurisdictions to date.⁸

Under Section 242, NCLT is vested with exclusive jurisdiction to deal with applications filed by member/s against oppression or mismanagement within the company. The NCLT's powers under the section extend to passing orders to the effect of regulating the affairs of the company, restrictions on the transfer of shares, removal of any of the directors of the company, etc.⁹ A member of a company can file such a complaint under Section 241.¹⁰

Despite these long-drawn, systematic reforms, the CA, 2013 omitted the definitions of the most categorical terms for the discussion in hand, namely "oppression" and "mismanagement". The subjective interpretations regarding the application and scope of Chapter XVI that have resulted from this omission gave rise to legal disputes and unresolved ambiguities. Against this backdrop, the Indian Courts have attempted to provide a comprehensive understanding of these legal principles within the Indian corporate framework.

A need for corporate restructuring can be felt by a company due to a series of reasons ranging from increasing market share, increasing market access, gaining benefits from economies of scale, reducing competition, etc. The impact of restructuring on the minority shareholders' rights depends on the terms and conditions agreed to by the company and the due diligence exercised.¹¹

Any decision taken by the company that is contrary to the interests of the minority shareholders is further exacerbated by certain inherent lacunas in Indian laws when it comes to providing

⁶ Ibid, s 430.

⁷ Ibid, s 434.

⁸ Shaneen Parikh and Namita Shetty, 'Protection and Redressal of Minority Shareholder Rights' (Cyril Amarchand Mangaldas Blogs, 6 March 2023) <https://corporate.cyrilamarchandblogs.com/2023/03/protection-and-redressal-of-minority-shareholder-rights/> accessed 5 January 2025.

⁹ The Companies Act 2013, s 242.

¹⁰ Ibid, s 241.

¹¹ Dennis C Mueller, 'Mergers and Market Share' (1985) 67 THE REV. OF ECON. & STAT. 256-267.

adequate protection to the minority at the stage of restructuring.¹²

What is Oppression?

Section 241(1)(a) provides that any member of a company or the Central Government can apply to the NCLT to complain about the company's affairs being conducted in a manner that is prejudicial to the public interest or oppressive to any member/s.¹³

The Hon'ble Supreme Court of India ("Supreme Court") has laid down the principles to be considered when considering the merits of a complaint of oppression in the case of *S.P. Jain v. Kalinga Tubes Ltd.*¹⁴

- i. The conduct must be cumbersome, pressurising and discriminatory.
- ii. The act should be over and above a lack of internal confidence amongst the members.
- iii. A lack of transparency and equal involvement of members exists.

These principles were built upon and elaborated in other cases. The Supreme Court has held that an isolated act would not qualify as oppression.¹⁵ *It is in line with preventing frivolous litigation.*¹⁶ *A lasting impact on the company or any member, when proven, acts as an exception.*¹⁷

In *Needle Industries India Ltd. v. Needle Industries Newey (India) Holdings Ltd.*, it was clarified that an illegal act, irrespective of its severity, does not amount to oppression without mala fide intention or instead of a harsh, burdensome, and wrongful act. On the other hand, the illegality of the act is not an essential ingredient for oppression, and the remedy can be availed under these provisions even when the act is lawful.¹⁸

In *V.S. Krishnan v. Westfort Hi-Tech Hospital Ltd.*,¹⁹ the Supreme Court further clarified that *the test to determining whether an action is oppressive in nature is not whether or not it was illegal but whether it fulfils the following conditions:*

- i. The conduct must be cumbersome, pressurising and discriminatory.

¹² Richard Rosecrance, 'Mergers and Acquisitions' (2005) 80 THE NAT'L INT'S 65-73.

¹³ Ibid, s 241(1)(a).

¹⁴ *S.P. Jain v. Kalinga Tubes Ltd. AIR 1965 SC 1535.*

¹⁵ *Sangramsinh P. Gaekwad v. Shantadevi P. Gaekwad [2005] 11 SCC 314.*

¹⁶ *K. Muthusamy v. S. Balasubramanian [2011] 167 Comp Cas 167.*

¹⁷ *Tea Brokers Pvt. Ltd. v. Hemendra Prosad Barooah [1998] 5 Comp LJ 463.*

¹⁸ *Needle Industries India Ltd. v. Needle Industries Newey India Holdings Ltd. 1981 3 SCC 333.*

¹⁹ *V.S. Krishnan v. Westfort Hi-Tech Hospital Ltd. 2008 3 SCC 363.*

- ii. An unfair advantage in the short-term would result.
- iii. The action is tainted with malice and bad intent.
- iv. The act being legal or illegal is not material.
- v. The remedial powers of the NCLT are wide once oppression is established.
- vi. Oppression is a question of fact to be determined on a case-to-case basis.

What is Mismanagement?

Section 241(1)(b) provides that any member of a company or the Central Government can apply to the NCLT to complain about the company's interest being conducted in a way prejudicial to its interest or to a shareholder or class of shareholders.²⁰ The Supreme Court in *K.R.S. Mani & Ors. v. Anugraha Jewellers Limited & Ors.*,²¹ read diversion of public money for unwanted purposes in a way that negatively affects the financial status of the company and in *Chander Krishan Gupta v. Pannalal Girdhari Lal Private Ltd.*,²² inaction against gross negligence in management affairs of the company into the scope of mismanagement under the section.

It was held in *Surinder Singh Bindra v Hindustan Fasteners Pvt Ltd.*,²³ that mismanagement can be said to be taking place as a result of an overhaul in the board of directors, alteration in the company's shareholding or membership, or any other material change becomes the reason for mismanagement within the company or when such material change is likely to lead to such mismanagement which is contrary to the public interest or the interests of the company or any shareholder or class of shareholders. The cause and effect between such material change leading to the alleged mismanagement have to be proved by the complainant to claim relief.²⁴ In *Jodh Raj Laddha v. Birla Corporation Ltd.*,²⁵ it was held that trivial changes, as against material changes, like imprudent decisions or decisions leading to a loss in business cannot amount to mismanagement under this section.

²⁰ The Companies Act 2013, s 241.

²¹ *K.R.S. Mani & Ors. v. Anugraha Jewellers Limited & Ors.* [2000] 100 Comp Cas 665.

²² *Chander Krishan Gupta v. Pannalal Girdhari Lal Private Ltd.* [1984] 55 Comp Cas 702.

²³ *Surinder Singh Bindra v Hindustan Fasteners Pvt Ltd.* 1990 69 Comp Cases 718.

²⁴ *Jodh Raj Laddha v. Birla Corporation Ltd.* [2011] 164 Comp Cas 238.

²⁵ *Ibid.*

What is Corporate Restructuring?

Corporate restructuring is the restructuring of the assets and liabilities of a company to maintain its cash flow needs, improve efficiency, promote growth and minimise cost. The implications for tax and legal liabilities need to be accounted for to make the restructuring successful. Some fundamental cultural and institutional changes also follow as a natural corollary. The effective implementation of changes is a long-term process.²⁶

Upon independence, India was a highly regulated economy for a considerable period. A lot of licenses and registrations were involved in setting up a company. This was infamously termed as the *license raj*. As a result of rigid regulatory requirements and government policies, it gave very limited leeway for corporate restructuring.²⁷

The economy started opening up with the Industrial Policy, 1991. It relaxed licensing and registration requirements and allowed foreign investments and technological transfer. Statutory reforms to allow the onset of liberalisation, globalisation, and privatisation, a restructuring of the Indian corporate structure started to keep up with the changes. This was in the global backdrop of a constantly globalising world aided by efforts of governments and organisations like WTO.²⁸

Today, restructuring is a commonplace, everyday, and widespread part of corporate functioning. A globalised economy and increasing competition are driving restructuring to occur faster than ever. M&A and takeovers of multinational corporate houses are a usual phenomenon. The removal of restrictions has made M&A operations lucrative to allow businesses to increase the scale of production with reduced costs at competitive prices. They also significantly contribute towards overall economic growth. Mergers allow companies to reduce the number of competitors and increase market share.²⁹

In the words of Justice D.Y. Chandrachud, “*Corporate restructuring is one of the means that can be employed to meet the challenges which confront business.*”³⁰

²⁶ *Mc Dowell & Company Limited v. The Commercial Tax Officer* 1986 AIR 649.

²⁷ Nimish Adhia, *The History of Economic Development in India since Independence* in India: Past, Present, and Future 18-22 (20th ed. 2015).

²⁸ *Ibid.*

²⁹ Anoop George and Shreya Bambulkar, A Need to Relook the Merger Control in the Digital Economy – An Analysis *Emerging Trends in Corporate and Commercial Laws of India* 03–23 (2019).

³⁰ *State Bank of India v. Rajesh Agarwal* [2024] 245 Comp Cas 623.

Consolidation of companies into fewer and larger entities leads to concentration in the economy. This keeps the global economy in a constant state of flux as companies constantly restructure and reposition themselves to position themselves as best as they can, according to the prevailing conditions in the economy.³¹

Corporate restructuring can take several forms:³²

- i. Mergers and acquisitions
- ii. Portfolio restructurings
- iii. Financial restructurings

The most commonly applied tools of corporate restructuring are:³³

- i. Amalgamation
- ii. Joint venture
- iii. Merger
- iv. Divestment
- v. Demerger
- vi. Slump sale
- vii. Acquisition

How does Corporate Restructuring impact the rights of Minority Shareholders?

Squeeze-out Mergers

A squeeze-out merger often adversely affects the interests of minority shareholders. A squeeze-out merger happens when the majority shareholders of a company gain ownership of the remaining shares, i.e. those held by the minority shareholders. They initiate a merger with another company. The majority shareholders, using their dominant position, dictate the details of the merger and force the minority shareholders of the original company to accept a 'fair price' for their shares, "freezing them out" from the restructured venture. The fairness of this 'fair price' is very difficult to establish.³⁴

³¹ Ibid.

³² Benu Singhal, Different Types of Corporate Restructuring <https://www.fe.training/free-resources/restructuring/different-types-of-corporate-restructuring/> accessed 5 January 2025.

³³ Ibid.

³⁴ Utkarsh Mani Tripathi, Evaluating Freezeout Mergers and Burden of Proof in Indian Corporate Law IRCCL Blog.

Profit maximisation is a very commonplace but flawed argument against the rights of minority shareholders. The world is increasingly incorporating factors like job satisfaction, happiness, etc., in accounting for the efficiency of the economy, which makes the supremacy of the interests of the company redundant as a utilitarian argument. Practices unreasonably compromising the interests of the minority shareholders need to be systematically done away with.³⁵

Section 236 of the Companies Act, 2013 provides for the procedure for the purchase of the shares of minority shareholders.³⁶ It creates a paradox of sorts. While the Companies Act, 2013 attempts to provide sufficient protection for the rights of minority shareholders, the language of the section is laid out in a way that encourages squeeze out.

Legal scholar Upendra Baxi has opined, “*litigation expenses borne by the dissenting shareholders are not worth the compensation they are receiving for giving up the shares. The price of the appraisal litigation, as compared to the likely profits along with the uncertainty involved, without any doubt, apprehends most of the minority shareholders from pursuing an appraisal remedy. Especially for a small shareholder, the cost of litigation overshadows the possible benefits of the ‘fair price’.*”³⁷

A ‘fair price’ option only comes into the scene when the compensation paid to minority shareholders is clearly insufficient. This makes it impossible to conclude this remedy as being sufficient to protect the minority shareholders.³⁸

Justice Katju has opined, “*This ex-post remedy is almost like a charity given by the majority after a request from the courts. It is only compensation and not protection for minority shareholders.*”³⁹

Still, this remedy is all that remains to date, and adequate measures for protecting the dissenting shareholders are still needed. Any other possible remedies come from judicial interpretation

³⁵ Anoop George and Shreya Bambulkar, Fair Value and Fair Price in Corporate Acquisitions 78 N.C. L. Rev. 101 (1999).

³⁶ The Companies Act 2013, s 236.

³⁷ M. Rishi Kumar Dugar, Minority Shareholders Buying Out Majority Shareholders - An Analysis 105-110 NLSIU L. Rev. Vol. 22 Issue 2 (2010).

³⁸ Ibid.

³⁹ Benu Singhal, Different Types of Corporate Restructuring

<https://www.fe.training/free-resources/restructuring/different-types-of-corporate-restructuring/> accessed 5 January 2025.

via judicial activism, but they are neither enough nor consistent.⁴⁰

The provisions of the Companies Act, 2013 allow majority shareholders to undertake a squeeze-out with ease, leaving the minority helpless against it. The subjective opinion of the minority shareholders concerning their stake in the company is not accounted for. They are squeezed out of the company in an unjustified manner.⁴¹

Sections 232 and 241 provide for an independent expert's assessment of the future merger⁴² and the option to approach a Court of law against oppression by the manner of the restructuring⁴³.

Statistical analysis depicts that more than 90% of such petitions for injunctions are rejected even without being afforded a hearing. Even more of them are rejected after initial hearings. It is a travesty of justice if the Court does not consider the case on merits and rejects the petition. This points towards the majority bias not just being limited to the statute but extending to judicial interpretations as well.⁴⁴

Misuse of the Proper Purpose Doctrine

With higher bargaining power, directors owe a fiduciary duty to the company in general and the minority shareholders in specific. More often than not, minority shareholders have to make do with trusting the majority shareholders' decisions in considering their interests. This makes transparency and bonafide decision-making very essential.⁴⁵

The doctrine is an extension of the famous quote, "With great power comes great responsibility". It mandates that directors must use their powers only for the purposes for which they have those powers and not misuse them. Majority shareholders misuse their fiduciary position during squeeze-out to make decisions detrimental to the interests of the minority shareholders.⁴⁶

⁴⁰ Ibid.

⁴¹ *Prakash Kadam v. Ramprasad Vishwanath Gupta & Anr* 2011 AIR SCW 3113.

⁴² The Companies Act 2013, s 232.

⁴³ Ibid, s 241.

⁴⁴ Akshat Sulalit, Companies Act, 2013: Rise of the Minority Shareholder I.L.J. Vol. 6 Issue 5 (2013).

⁴⁵ Ibid.

⁴⁶ *Eclairs Group v. JKX Oil* [2015] UKSC 71.

The failure to disclose the requisite information at the appropriate time amounts to a breach of trust. Unfortunately, there is neither any provision to this effect in the Companies Act, 2013 nor reflected often in the Courts' judgement in India.⁴⁷

Slump Sales and Insertion of Regulation 37A

In India, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR")⁴⁸ and the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018⁴⁹ regulate M&A transactions.

Regulation 37 of the LODR requires companies to acquire a no-objection letter from the stock exchange before going through with a merger. This no-objection certificate has to be placed before the NCLT for approval. Among other things, the NCLT is expected to scrutinise the impact on shareholders' rights, although it is not an essential criterion for the NCLT to provide its approval.⁵⁰

An amendment to the LODR in 2023 inserted Regulation 37A as an exception to Regulation 37. It covers private transactions like slump sales. A slump sale is a Business Transfer Agreement (BTA) in India, which is the transfer of assets and liabilities in exchange for a lump sum amount. Regulation 37A requires listed companies to obtain the members' approval through a special resolution and disclose the underlying reasoning behind the private transaction. The important caveat is that the special resolution has to be approved by a majority of the minority shareholders. This effectively gives the minority shareholders the right to decide whether the transaction should go through.⁵¹

It would take away from the compromising stance taken under Section 188 of the Companies Act, 2013 by the legislature, allowing minority shareholders' opinions to be not accounted for to avoid a 'conflict of interest' in business transfer decisions. It gives minority shareholders the power to block special resolutions which jeopardise their interest in the company.⁵²

That being said, a balance needs to be struck between minority rights and allowing the smooth

⁴⁷ Ibid.

⁴⁸ SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015.

⁴⁹ SEBI (Issue of Capital and Disclosure Requirements) Regulations 2018.

⁵⁰ SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015, Regulation 37.

⁵¹ Ibid, Regulation 37A.

⁵² The Companies Act 2013, s 188.

functioning of the company. The blanket requirement of minority approval under 37A might lead to practical issues where minority shareholders may block even genuine transactions.

Conclusion

The CA, 2013, has been brought about for the herculean task of steering, regulating, and stabilising the labyrinthine corporate system in India. Chapter XVI, which deals with the issues of oppression and mismanagement within a company, forms a very important part of the statute.

The stake held by the minority shareholders in a company is not subject to the whims and fancies of the majority shareholders of that company. In line with that spirit, the rights of the minority shareholders have been accorded protection against oppression and mismanagement at the hands of the majority shareholders under the CA, 2013. The NCLT and NCALT have adequate powers to grant relief to minority shareholders.

The meaning of the terms ‘oppression’ and ‘mismanagement’ have been subject to discussion in several landmark judgements due to not being defined under Chapter XVI despite their significance in the corporate world. Although this can be termed as a shortcoming on the part of the lawmakers, the Courts have done a fine job in delineating the constituents of ‘oppression’ and ‘mismanagement’. The Courts have interpreted these terms in the light of law, justice, and commerce, plugging loopholes wherever possible. Oppression, beyond mere disagreement, has been interpreted to entail burdensome, harsh, and wrongful conduct along with a lack of fair dealing and a sustained pattern of oppressive behaviour. Mismanagement, on the other hand, entails conducting the affairs of a company in a prejudicial, and inept manner jeopardising the interests of minority shareholders. In a splendid display of flexibility and adaptability, the Indian legal system has ensured effective enforcement of the remedies under Chapter XVI despite the inherent shortcomings in the Chapter.

A balance between the tyranny of the majority and the smooth functioning of the company is a herculean but possible task. Minorities must not be treated as expendables and must be accorded adequate protection without replacing majoritarian tyranny with minority dominance. There can be a slew of motivations and interests that may not be justified solely via a ‘fair price’ compensation. The Indian laws are ignorant of the same, and no judicial precedent exists. Fairly protecting the rights of the minority shareholders while ensuring the objectives of the company are not compromised is possible. It is just the requisite will that is missing.